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DIRECTORATE OF
INTELLIGENCE

Intelligence Memorandum

*Developments in Communist Petroleum Trade
with the Free World : 1968 and Prospects for 1969-70*

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CENTRAL INTELLIGENCE AGENCY
Directorate of Intelligence
April 1969

INTELLIGENCE MEMORANDUM

Developments in Communist Petroleum Trade
with the Free World:
1968 and Prospects for 1969-70

Summary

In 1968 the USSR failed to increase its petroleum exports to the Free World for the first time since 1955, and little expansion is likely at least through the mid-1970's. Soviet exports consisted of 26 million tons of crude oil and 17 million tons of petroleum products. Eastern European countries exported about 8 million tons of petroleum products to the Free World, one million tons more than in 1967. Together the Communist countries* delivered 51 million tons of petroleum valued at about \$700 million in 1968. About 85 percent of these deliveries went to developed countries and earned about \$500 million in hard currencies. Soviet exports to the less developed countries declined for the third successive year.

Exports of oil from the USSR to markets east of Suez continued to show some effect of the higher transport costs resulting from closure of the Canal. The quantity of oil sold to Japan, the principal market affected, which had declined nearly 900,000 tons in 1967, fell an additional 300,000 tons in 1968. This decline would have been greater if the USSR had not participated in swap arrangements with

* All references to exports of petroleum from Communist countries refer to exports from the USSR and the Communist countries of Eastern Europe -- Bulgaria, Czechoslovakia, East Germany, Hungary, Poland, and Rumania.

Note: This memorandum was produced solely by CIA. It was prepared by the Office of Economic Research.

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Western oil companies. Under this procedure, Free World companies provide oil to the USSR at Persian Gulf terminals for Soviet markets east of Suez. In exchange, the USSR delivers oil at Black Sea ports to these companies for their markets in Western Europe. This arrangement, which saves transport costs, probably will be continued and expanded even after the Canal is reopened.

The Eastern European countries, except Rumania, continued to depend on the USSR for about 85 percent of their oil supply. Their exports of petroleum products (about 4 million tons, mainly to Western Europe), in effect, are derived from Soviet crude oil. Dependence on Soviet oil will not diminish significantly through the mid-1970's in spite of the efforts of several of the countries to obtain new sources of oil in the Middle East. Rumanian exports of petroleum products (about 4 million tons in 1968) have been derived from Rumanian crude oil. Little or no increase in domestic crude oil production is expected, however, and in order to expand its exports, Rumania hopes to increase its supply of crude oil by means of agreements concluded with Iran, Saudi Arabia, and Venezuela to exchange industrial goods for oil.

The growth of Soviet oil production has slowed and may diminish further during the next few years. Costs of production are increasing in the established oilfields, and development of new fields has been slow and will be expensive. With commitments to Eastern Europe and domestic demand rising rapidly, the USSR probably will be unable to increase oil exports to the Free World in the next few years. In 1969 these are likely to decline by about 4 million tons (10 percent) to about 39 million tons, and only a partial recovery can be expected in 1970. The USSR may obtain small quantities of oil from national oil companies in the Middle East and Africa through barter of industrial goods and use such oil to maintain its position in Free World markets. Even though exports from the Eastern European countries, especially Rumania, should rise, total Communist oil exports to the Free World in 1969 and 1970 probably will not significantly exceed the 1968 level. The share of Free World demand (excluding the United States) that Communist countries will satisfy in 1969-70, consequently, will decline to less than 5 percent, compared with 5 to 6 percent in recent years.

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Origin and Composition of Oil Exports

1. The USSR and the Communist countries of Eastern Europe exported about 51 million tons* of petroleum to the Free World in 1968, valued at about \$700 million, an increase of less than 1 million tons, or 2 percent, over 1967. Exports from the USSR amounted to 43 million tons (\$540 million) -- more than 26 million tons of crude oil and about 17 million tons of petroleum products -- and were slightly less than in 1967. Hard-currency markets accounted for about \$375 million of Soviet exports and \$140 million of Eastern European exports.

2. The year 1968 was the first one in which the USSR failed to increase its oil exports to the Free World since becoming a net exporter in 1955. Soviet crude oil production in 1968 rose 21 million tons, or 7 percent -- a rate of growth considerably below the average of 10 percent during 1961-67 -- whereas domestic demand increased almost 9 percent and exports to Eastern Europe increased about 14 percent.

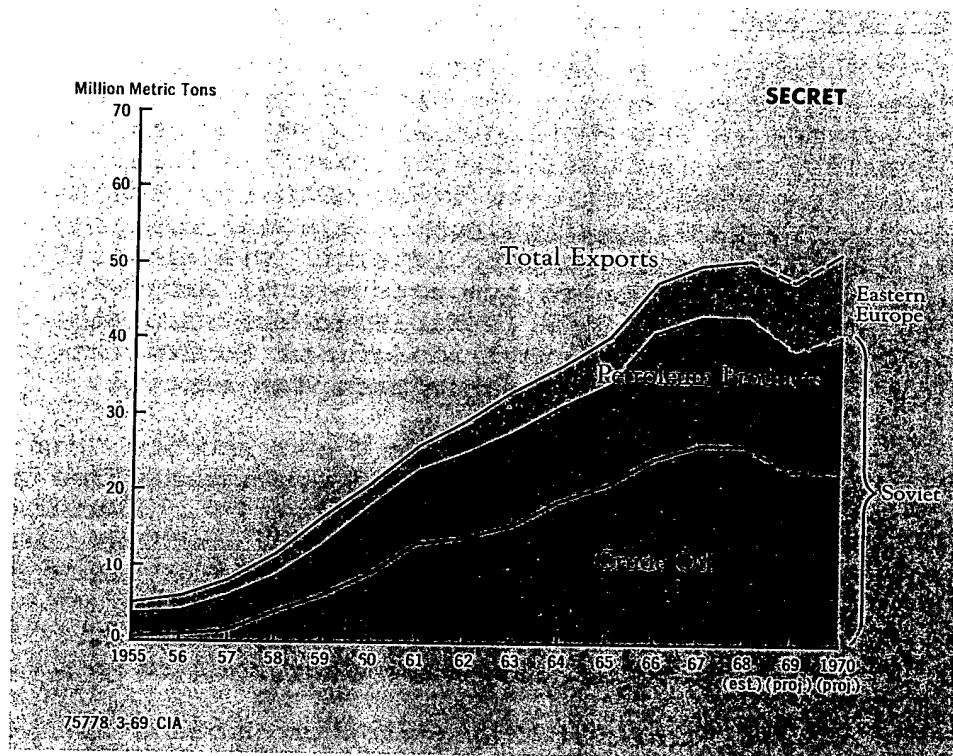
3. The Communist countries of Eastern Europe exported 8 million tons of oil to the Free World in 1968. These exports, all in the form of petroleum products and valued at \$160 million, were responsible for the increase of 1 million tons in total Communist deliveries. Rumania was the largest Eastern European supplier, exporting 4 million tons of products derived from domestic crude oil. The other Eastern European Communist countries** exported petroleum products derived mainly from Soviet crude oil. Exports of petroleum from Communist countries to the Free World since 1955 are shown in the following chart.

* All tonnages are metric tons.

** The remaining 4 million tons from Eastern Europe consisted of about 1 million tons each from Czechoslovakia, Hungary, and Poland, 600,000 tons from East Germany, and 300,000 tons from Bulgaria.

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4. At least 90 percent of the petroleum exported from the Communist countries to the Free World in 1968 was shipped in tankers -- more than half in Communist-flag ships. About 32 million tons of the exports originated from Black Sea ports, an increase of 2 million tons over 1967. Baltic Sea ports accounted for almost 15 million tons, about the same as last year. The remainder was shipped from ports in the Soviet Far East or by rail and barge, as shown in the following tabulation for 1968:

Export Movement	Million Tons				Percent of Total
	From the USSR		Petroleum Products from Eastern Europe	Total	
	Crude Oil	Petroleum Products			
Black Sea ports	16.8	11.0	4.6	32.4	63
Baltic Sea ports	8.2	5.5	0.9	14.6	28
Far Eastern ports	0.8	0	0	0.8	2
Rail and barge	0.7	0.3	2.5	3.5	7
Total	26.5	16.8	8.0	51.3	100

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Destination of Exports

5. The USSR and, to a lesser degree, Rumania made minor adjustments in their pattern of oil exports in 1968 in order to maintain markets in the hard-currency countries. The increased cost of transport resulting from the closure of the Suez Canal brought about a total decline of about 1.1 million tons in exports to Japan, India, and Ceylon in 1968. The drop in exports to Japan was about 800,000 tons, and the share of Japan's oil supply coming from Communist countries fell to about 2 percent from more than 3 percent in 1967. Shipments to Western Europe rose by 1.8 million tons, and Communist countries provided about the same share of total oil supply in Western Europe (9 percent) in 1968 as in 1967. Table 1 shows the Free World destinations of oil exports from Communist countries in 1968.

6. The decline in exports to the less developed countries that has occurred each year since 1965 is expected to continue in the next few years. A substantial decrease is anticipated in exports to the two largest markets in this category -- Egypt, where domestic production soon will make that country self-sufficient, and Greece, which recently concluded a long-term contract with Western oil companies for most of its oil requirements through 1980. The following tabulation shows Communist oil exports to developed and less developed countries in 1967-68:

<u>Importing Area</u>	<u>Million Tons</u>					
	<u>1967</u>			<u>1968</u>		
	<u>From the USSR</u>	<u>From Eastern Europe</u>	<u>Total</u>	<u>From the USSR</u>	<u>From Eastern Europe</u>	<u>Total</u>
Developed countries	<u>37.2</u>	<u>6.0</u>	<u>43.2</u>	<u>37.6</u>	<u>6.8</u>	<u>44.4</u>
Western Europe	33.9	5.2	39.1	34.6	6.5	41.1
Japan	3.3	0.8	4.1	3.0	0.3	3.3
Less developed countries	<u>6.3</u>	<u>0.9</u>	<u>7.2</u>	<u>5.7</u>	<u>1.2</u>	<u>6.9</u>
Total	43.5	6.9	50.4	43.3	8.0	51.3

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Oil Imports from the Free World

7. In an effort to expand trade and to diversify to a small degree their sources of oil supply, Eastern European Communist countries in 1968 negotiated barter arrangements with countries in the Middle East and with Venezuela. Rumania, expecting to export more refined products but faced with little or no growth in output of crude oil, concluded barter agreements to import 9 million tons of crude oil from Saudi Arabia and 3.5 million tons from Iran through 1972. Rumania also signed an agreement in principle with the government-owned Venezuelan Petroleum Company to supply 11 million tons of petroleum during 1969-78 in exchange for \$125 million of machinery and equipment. Moreover, Rumania made spot purchases of 150,000 tons of crude oil for cash in 1968 from US concessionaires in Libya.

8. After the delivery of about 350,000 tons of crude oil via the Cape of Good Hope in 1968, Saudi Arabia discontinued exports to Rumania pending a decision as to how the Rumanian credits could best be used. It is possible, however, that this action was related to Saudi Arabia's anti-Israeli attitude. Iran's exports of 250,000 tons of crude oil to Rumania in 1968 were moved through the existing trans-Israel pipeline from the Gulf of Aqaba to the Mediterranean for further movement to Rumania.

9. In early 1968, Hungary and Czechoslovakia signed barter agreements with Iran for the import of oil, but no details have been published. Both countries are land-locked, and prohibitive transport costs may militate against implementation. For political reasons, these countries apparently are unwilling to use the Israeli pipeline to reduce transport costs. Moreover, the line presently is being fully utilized for Israeli and Rumanian needs. Yugoslavia is constructing a crude oil pipeline from a port on the Adriatic Sea to serve domestic refineries and has proposed that Hungary and Czechoslovakia extend the line north to serve their needs. Although both Hungary and Czechoslovakia reportedly agreed to this project, financing has apparently been a problem, and the proposal has been held in abeyance. Construction of the Yugoslav segment of the line is continuing, and negotiations could be resumed.

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10. Bulgaria, East Germany, and Poland, all readily accessible by sea, have not sought Free World oil as aggressively as the other Eastern European countries. Bulgaria did conclude a barter arrangement with Iran in 1967 to import 2.3 million tons of crude oil during 1968-70, but the Suez closure prevented implementation. Bulgaria also concluded agreements with Algeria and Syria and received small quantities of oil from both sources in late 1968. East Germany has imported about 150,000 tons of crude oil annually from the UAR for several years but has neither concluded nor sought barter arrangements with other Middle East countries. Poland has not imported crude oil from the Free World and apparently has no immediate plans to do so.

11. The USSR itself entered into a long-term trade agreement with Algeria in 1968 that includes Soviet delivery of manufactured goods to Algeria in return for Algerian crude oil. The USSR may decide to deliver the oil to Ghana, Morocco, and perhaps others, while conserving its own oil for sales to hard-currency countries.

East-West Oil Exchanges

12. The oil exchanges inaugurated by the USSR and certain Western oil companies in late 1967 to overcome the higher transport costs arising from the Suez Canal closure were expanded in 1968. Under this arrangement, Western oil companies provide oil to the USSR at Persian Gulf sources for delivery to Soviet markets east of Suez. In exchange, the USSR provides oil to the Western oil companies at Black Sea ports for delivery to their markets in Europe. The following exchanges reportedly were negotiated in 1968:

<u>Source in Persian Gulf</u>	<u>Quantity (Thousand Tons)</u>	<u>Period</u>
British Petroleum	750 to 1,000	Jul 68 to Feb/Jun 69
Compagnie Française Des Pétroles (C.F.P.)	500	Jun 68 to Dec 68

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13. Egypt also may be involved in an oil exchange involving the USSR and Japan. Oil from the UAR's Morgan field in the Gulf of Suez, where production is increasing rapidly, cannot now be moved economically to the refinery at Alexandria while the Canal remains closed. There is evidence that 500,000 tons of this Morgan crude oil will be moved to Japan in 1969 against the Japanese-Soviet account. In exchange, a corresponding quantity of Soviet crude oil will be delivered to Alexandria.

14. The mutually beneficial oil exchanges that the USSR has negotiated since the closure of the Suez Canal may continue after the Canal is reopened and even if the proposed Suez-to-Mediterranean pipeline through Egypt is constructed. In addition to preserving Soviet markets that might otherwise be lost because of the higher transport costs, the oil exchanges permit the USSR to use its tanker fleet more effectively, and the importing countries benefit from lower landed costs. The quantities involved, however, are small -- at its peak level in 1966, the USSR exported six million tons of oil east of Suez -- and they represent only a small part of the total oil imports in the area east of Suez.

Soviet Investment in Free World Oil Activities

15. The USSR, which hitherto had limited its internal marketing activities abroad to Great Britain, expanded them to Belgium in 1968. Previous Soviet participation in Free World oil activities had been restricted essentially to sales of crude oil and refined products at marine terminals and to the provision of technical assistance and equipment for oil industries in the less developed countries. Only in Great Britain had the USSR invested in the ownership of local distribution facilities.

16. The establishment of a joint Soviet-Belgian company -- Nafta (B) -- at the outset of 1968 was more ambitious in scope. The firm, capitalized initially at a modest \$60,000 and owned 60 percent by Soviet agencies and 40 percent by private Belgian interests, was authorized to engage in all activities related to petroleum and began construction of an import and distribution facility in the Antwerp harbor area in 1968. Moreover, the firm reportedly was interested in buying or building a refinery in the area, the first evidence of Soviet interest in

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this kind of activity, but as yet nothing has come of this.

17. In late 1968 the Soviet oil exporting organization, Soyuznefteksport, was seeking to establish a joint marketing enterprise in France similar to Nafta (B). France has imported between 2.5 and 3 million tons of crude oil and petroleum products annually from the USSR for the past three years (1966-68).

Prospects for Oil Trade in 1969 and 1970

18. Soviet oil exports to the Free World are unlikely to increase much, if at all, through the mid-1970's. The rate of growth of Soviet crude oil production may decline further because of increasing costs in existing fields and the slow progress and high cost of developing new fields. At the same time, Soviet domestic demand is likely to grow at 7 to 8 percent annually, and Soviet exports to Eastern Europe will be greater than originally planned as a result of the decision to continue supplying the predominant part of the region's oil requirements until at least 1975.

19. Production of crude oil in the USSR in 1969 and 1970 apparently will be less than was originally anticipated. In 1969, output of crude oil is to reach 326.5 million tons, only about 17 million tons more than in 1968 and the smallest absolute increase since 1959. The goal for 1970 recently has been cited as between 346 and 350 million tons. Preliminary estimates for 1969 indicate that a total of about 83 million tons of petroleum -- 59 million tons of crude oil and 24 million tons of products -- will be available for export in 1969. Soviet exports to other Communist countries, primarily Eastern Europe, will increase from about 39 million tons in 1968 to about 44 million tons in 1969. Thus supplies of oil available for export to the Free World in 1969 will approximate 39 million tons, or 4 million tons less than in 1968. In 1970, total Soviet oil available for export probably will be about 6 million tons more than in 1969. Most of this additional oil, however, will go to other Communist countries, and Soviet exports to the Free World in 1970 may be about 5 percent above the level of 1969, but still less than in 1968. A forecast of Soviet exports of

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oil by market groups during 1969-70 is shown in the following tabulation:

Destination	Million Tons					
	1969			1970		
	Crude Oil	Petroleum Products	Total	Crude Oil	Petroleum Products	Total
Free World	23	16	39	23	18	41
Other Communist countries	36	8	44	42	6	48
Total	59	24	83	65	24	89

Estimates of Soviet exports to individual Communist countries during 1967-68 and projected exports for 1969-70 are shown in Table 2.

20. The decrease in Soviet exports of oil to the Free World in 1969 and 1970 will be partly offset by an increase in exports of petroleum products from Eastern Europe, but total Communist exports of oil to the Free World probably will fall slightly in 1969 and return in 1970 to about the level of 1968. If total Communist oil exports to the Free World remain unchanged while Free World demand increases at the expected annual rate of 7 to 8 percent, Communist oil as a share of Free World demand (excluding the United States) will decline to less than 5 percent in 1969-70, compared with between 5 and 6 percent in 1967-68.

21. The Eastern European Communist countries, except Rumania, will continue to obtain the overwhelming share of their oil needs from the USSR, at least through the mid-1970's. The Friendship crude oil pipeline system, which links Poland, East Germany, Czechoslovakia, and Hungary with the oilfields of the Urals-Volga region of the USSR, currently is being expanded. The northern and southern sections of the Friendship pipeline to Eastern Europe will have a combined annual capacity of 45 to 50 million tons in 1974 or 1975 when all pumping stations are in operation. If, as is likely, the line is operated near

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optimum capacity, it will supply enough Soviet crude oil to cover about 80 percent of total demand in the four Eastern European countries served by the line. This would leave only about 10 percent of their requirements to be supplied from Free World sources.

22. In effect, therefore, most of Eastern Europe's exports of oil products to the Free World (except those of Rumania) will continue to be derived from Soviet crude oil. Unable to increase its own oil exports to the Free World, it is unlikely that the USSR will permit the Eastern European countries to expand their exports very much, as this would amount to a considerable diversion of hard currency that the USSR also needs.

23. Rumania is an exception because the prospective increase in Rumanian exports of petroleum products will be derived, at least indirectly, from crude oil imported from the Free World. Rumania will have sufficient refining capacity in excess of domestic crude oil production to process about 3 million tons of imported oil by 1970 and 6 to 7 million tons by 1975. Exports of products from Rumania will account for an estimated two-thirds of the total increase in exports of petroleum products from Eastern Europe through 1970.

24. In order to maximize earnings of hard currency, the USSR probably will direct its Free World exports of indigenous oil almost exclusively to industrialized countries. Oil supplied to the less developed countries may be on the basis of barter deals such as the one with Algeria, described above.

25. In the long term, if sufficient investment is allocated to the petroleum industry, the USSR's ample resources of petroleum can be developed. In the meantime, the USSR may attempt to maintain its position in Free World markets by obtaining small quantities of oil from national oil companies in the Middle East or Africa through barter deals, as repayment for past credits, or by acting as broker for oil not under control of established oil companies in countries such as Syria, Egypt, Iran, and Iraq. There is no evidence that the USSR will, in the next year or two, step up its procurement of oil from the Middle East sufficiently to pose a threat to Free World interests.

Table 1

Communist Exports of Petroleum to the Free World a/
1968

Destination b/	Thousand Metric Tons					Percent of Recipient's Demand
	Crude Oil from the USSR	Petroleum Products			Total Petroleum	
		From the USSR	From the Eastern European Communist Countries	Total		
Total	26,470	16,770	8,020	24,790	51,260	7 c/
Western Europe	22,100	12,850	6,470	19,320	41,420	9
Austria	700	300	1,900	2,200	2,900	41
Belgium	0	600	200	800	800	4
Denmark	0	550	300	850	850	6
Finland	5,000	2,400	250	2,650	7,650	90
France	1,600	1,000	1,100	2,100	3,700	5
Iceland	0	450	0	450	450	82
Ireland	0	200	0	200	200	6
Italy	10,500	1,100	600	1,700	12,200	18
Netherlands	0	150	0	150	150	Negl.
Norway	0	400	50	450	450	7
Spain	300	20	0	20	320	1
Sweden	0	4,100	500	4,600	4,600	19
Switzerland	0	150	450	600	600	6
United Kingdom	0	30	20	50	50	Negl.
West Germany	4,000	1,400	1,100	2,500	6,500	6
Middle East	1,700	1,500	930	2,430	4,130	20
Cyprus	0	150	0	150	1,150	33
Greece	600	550	450	1,000	1,600	28
Syria	0	200	160	360	360	22
Turkey	0	200	70	270	270	5
United Arab Republic	1,100	400	250	650	1,750	27

Table 2

Soviet Exports of Petroleum to Other Communist Countries a/

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Importing Area	Million Metric Tons					
	1967			1968 (Estimated)		
	Crude Oil	Petroleum Products	Total	Crude Oil	Petroleum Products	Total
Eastern Europe	22.6	4.9	27.6	26.3	5.1	31.4
Bulgaria	2.7	1.8	4.5	3.1	2.0	5.1
Czechoslovakia	7.4	0.5	7.9	8.0	0.3	8.3
East Germany	6.1	0.1	6.3	6.6	0.1	6.7
Hungary	2.8	0.6	3.4	3.0	0.5	3.5
Poland	3.6	1.9	5.5	5.6	2.2	7.8
Rumania	0	Negl.	Negl.	0	Negl.	Negl.
Far East	Negl.	0.8	0.9	Negl.	1.0	1.0
Communist China	0	Negl.	Negl.	0	Negl.	Negl.
Mongolia	Negl.	0.2	0.2	Negl.	0.2	0.2
North Korea	0	0.4	0.4	0	0.5	0.5
North Vietnam	0	0.2	0.2	0	0.3	0.3
Other	4.6	2.2	6.8	4.7	1.9	6.7
Cuba	3.8	1.4	5.3	4.0	1.3	5.3
Yugoslavia	0.7	0.8	1.5	0.7	0.6	1.4
Total	27.3	8.0	35.3	31.0	8.0	39.0
				36.2	7.9	44.1
				41.8	6.4	48.2

a. Because of rounding, components may not add to the totals shown.

Table 1

Communist Exports of Petroleum to the Free World a/
1968
(Continued)

Destination b/	Thousand Metric Tons					Percent of Recipient's Demand
	Crude Oil from the USSR	Petroleum Products			Total Petroleum	
		From the USSR	From the Eastern European Communist Countries	Total		
Africa	650	180	40	220	870	28
Ethiopia	0	0	20	20	20	6
Ghana	100	0	0	0	100	15
Guinea	0	90	0	90	90	33
Morocco	550	0	0	0	550	35
Senegal	0	40	20	60	60	25
Somalia	0	50	0	50	50	95
Asia	1,620	2,230	490	2,720	4,340	3
Afghanistan	0	130	0	130	130	40
Burma	20	0	0	0	20	2
Ceylon	0	300	140	440	440	33
India	0	400	50	450	450	3
Japan	1,600	1,400	300	1,700	3,300	2
Latin America	400	10	20	30	430	2
Brazil	400	0	0	0	400	2
Colombia	0	0	20	20	20	Negl.
Uruguay	0	10	0	10	10	Negl.
North America	0	0	70	70	70	Negl.
United States	0	0	70	70	70	Negl.

a. Preliminary estimates derived primarily from information on tanker movements and from Free World import data.

b. [REDACTED] indicates a less developed country; all others are developed countries.

c. Percent of demand for countries listed, excluding the United States. Oil from Communist countries represented between 5 and 6 percent of total demand in the Free World, excluding the United States.